

3861

(b)(1)
(b)(3)
(S)

~~Secret~~

MICRO

~~NOFORN NOCONTRACT~~
~~ORCON~~

CIAALA --- AR-94-002 ---

16 FEB 1994



Directorate of Intelligence

FILM PER C/CIA LIBRARY

Africa Review

*Special Issue: Impact of CFA
Devaluation in Francophone Africa*

4 February 1994

APPROVED FOR RELEASE
DATE: OCT 2001

~~Secret~~

ALA AR 94-002
4 February 1994

Copy 244

D
30

~~Secret~~
~~NOFORN-NOCONTRACT~~
~~ORCON~~

Africa Review

Special Issue: Impact of CFA Devaluation in Francophone Africa

4 February 1994

Articles	Page
Francophone Africa and the CFA Franc Devaluation: A Regional Perspective	1
<p>In the short term, the main economic benefit of the devaluation is likely to be a net foreign capital inflow for the African CFA countries. There is concern, however, about a backlash from key urban groups and the military, and some CFA governments have already imposed price controls or rolled back some austerity measures.</p>	
Cote d'Ivoire: Facing a Tough Time Selling Devaluation	9
<p>Newly installed President Bedie is likely to face increased pressure to give economic concessions to key political constituencies, a situation that could undermine the benefits of the devaluation to Cote d'Ivoire as a major regional labor market and exporter.</p>	
Senegal: Diouf's Risky Turnabout	13
<p>Long an outspoken critic of devaluation, President Diouf faces his most difficult political challenge as he seeks to build support for economic reforms that will be painful for important urban groups whose sympathies lay with the political opposition.</p>	
Cameroon: Government Ill-Prepared To Take Advantage of Devaluation	19
<p>Of the CFA franc zone's larger economies, Cameroon is probably the least able to take advantage of the potential benefits of the devaluation to halt its economic slide. Without an infusion of international aid, shortages of consumer goods and worsening living conditions are likely to trigger civil unrest.</p>	

~~Secret~~
~~NOFORN NOCONTRACT~~
~~ORCON~~

Benin: Putting Fragile Democracy to the Test [REDACTED]

23

[REDACTED]

President Soglo's determined pursuit of economic reform has been rewarded with three straight years of economic growth, and he is likely to press forward with reforms despite the potential political backlash caused by the devaluation. [REDACTED]

Gabon: Devaluation Likely To Have Few Benefits [REDACTED]

25

[REDACTED]

With one of Sub-Saharan Africa's strongest economies, Gabon is unlikely to benefit much economically from the CFA devaluation, but it will face many of the same political risks as its franc zone neighbors. [REDACTED]

Mali: Sharing the Pie Among Noisy Economic Interests [REDACTED]

29

[REDACTED]

Although the government hopes to continue reform measures that will foster diversification of the economy and attract foreign investment, widespread unrest that could follow the devaluation may force President Konare to backtrack on key austerity measures. [REDACTED]

[REDACTED]

[REDACTED]

~~Secret~~

~~Secret~~
~~NOFORN NOCONTRACT~~
~~ORCON~~

Africa Review (U)

Articles

Francophone Africa and the CFA Franc Devaluation: A Regional Perspective

The recent devaluation of the African Franc Zone (CFA) franc marks a shift in the tenor of the financial arrangements between France and its former African colonies. Although devaluation was a bitter pill for Paris to swallow, it realized that the subsidies needed to maintain the historic exchange rate would have continued to grow. For the Africans, an overvalued CFA franc was a boon to influential urban elite groups, but hobbled economic growth. In the short term, the main economic benefit of the devaluation is likely to be a net foreign capital inflow for the African CFA countries. The CFA governments are concerned, however, about the potential for a backlash from key urban groups and the military, and some have already imposed temporary price controls or partly rolled back recent austerity measures. These steps reflect political realities, but, if taken to extreme, would fritter away the benefits of devaluation. The long-term impact of the devaluation will depend on conditions in each country and on the willingness and ability of the CFA leaders to follow through with further economic reforms. Meanwhile, donors face a daunting task of maintaining pressure for further reform, while trying to judge the capability of each country to absorb it.

Backdrop to Devaluation

French and African officials involved in the Franc Zone, a monetary area that involves France and 14 African countries, took pride in the stability of the CFA franc, which traded for more than 45 years at a rate of 0.02 French franc per CFA franc.¹ Paris guaranteed its

convertibility and credited the fixed exchange rate with imposing fiscal and monetary policy discipline on African member countries and with keeping their inflation rates relatively low. Under CFA rules, the African governments could not resort to printing money ad infinitum to cover deficit spending. Moreover, with a fixed exchange value of the CFA franc, any fall in export earnings reduced government revenues through lower tax and import duty collection and, absent more foreign aid or loans, theoretically forced spending cuts. The CFA economies have done better than those of other West African states in containing money supply growth and inflation rates (see Figure 2). They have, however, only matched their neighbors' poor performances in restraining foreign debt accumulation.

Officials from the IMF and World Bank argued for years that the CFA franc was overvalued and pressed the CFA countries to improve their "competitiveness"—a codeword for the politically sensitive issue of devaluing the CFA franc. In our view, this overvaluation resulted from a combination of declining world prices (in dollars) for some important CFA commodity exports—such as coffee and cocoa—and a rise in the dollar value of the French franc. The weak commodity prices and overvalued currency have hurt farmers and other export-oriented producers in African CFA countries and have driven many marginal participants out of the market economy. As a result, the CFA economies have performed worse than their neighbors in terms of average economic growth rates.

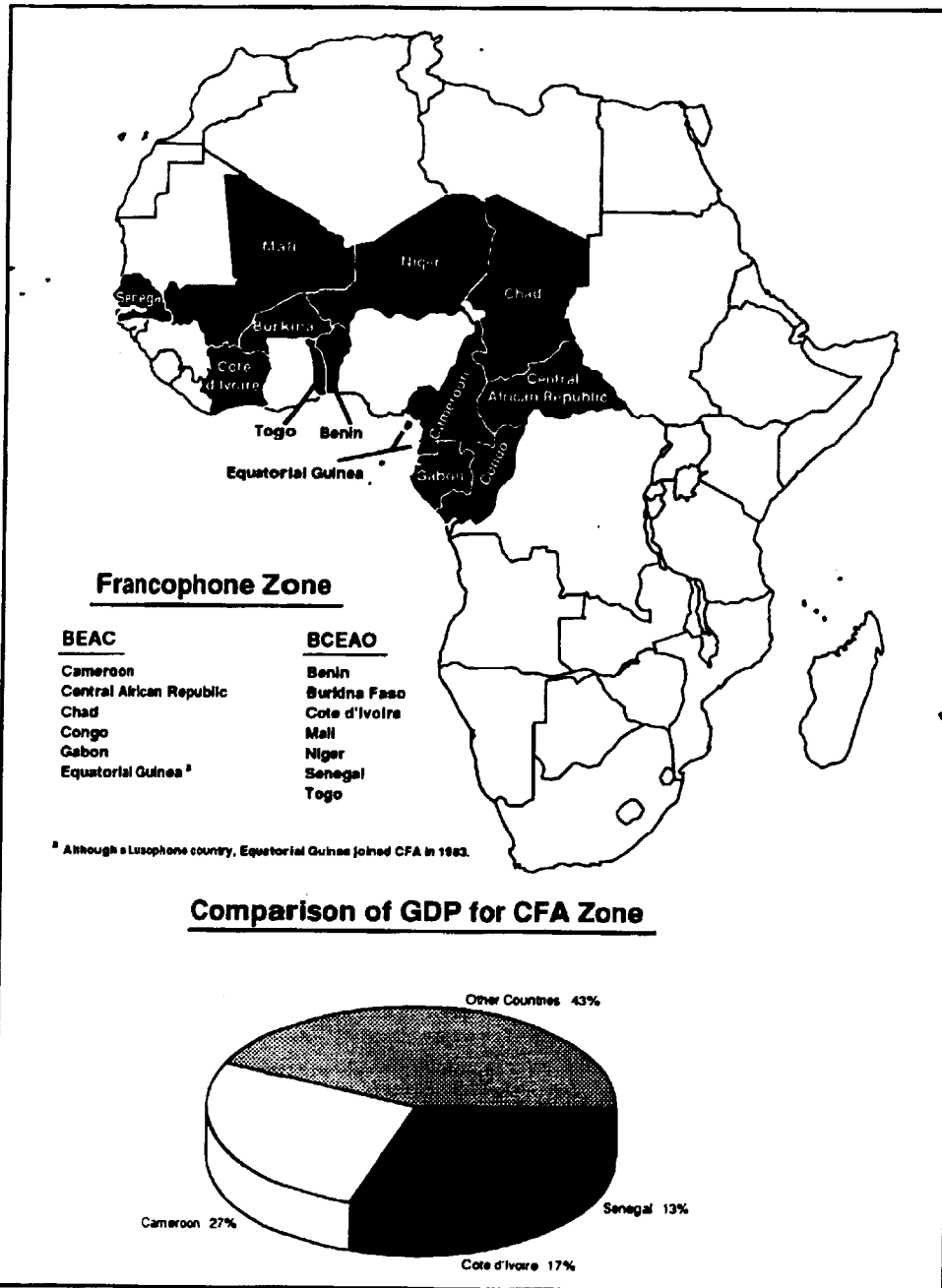
Recognition that the CFA franc was overvalued also sparked capital outflows from the African CFA countries. Many firms and individuals with assets in

¹The Franc Zone comprises two monetary unions—the West African Monetary Union (the Communauté Financière Africaine) and the Central African Customs and Excise Union (the Coopération Financière en Afrique Centrale)—that each issue a currency. The currencies collectively are called the CFA franc. Comoros participates, but issues its own franc that now is fixed at an exchange rate of 75 Comoros francs per French franc.

~~Secret~~

POOR QUALITY PAGE

Figure 1

African Franc Zone States~~Secret~~

~~Secret~~

CFA countries worried about the impact of a devaluation on the value of those assets and took advantage of free convertibility of the CFA franc to move wealth elsewhere. The CFA countries responded last August by restricting capital outflows—such as the conversion of CFA currency outside of the African CFA countries—but apparently with little effect. [REDACTED]

Even as the CFA governments grew to accept the inevitability of a devaluation, they postponed it repeatedly—largely because they feared a backlash from urban and military elites. For these groups, an overvalued CFA franc made their luxury imports cheaper. As one observer astutely noted, the overvalued CFA franc favored French champagne over Ivorian cocoa. Many of the affected elites probably believed that they had a tacit understanding with the political leaders of their countries to protect their economic interests through job security and above-market salaries in exchange for their political support or at least quiescence. [REDACTED]

Short-Term Capital Inflows, But Threat of a Backlash

In our judgment, the devaluation of the CFA franc on 12 January by 50 percent to a new rate of 0.01 CFA franc per French franc will benefit virtually all of the African CFA economies in the short-run, albeit to varying degrees and in differing ways, depending on local conditions. Unless unrest flares, they will reap short-term net inflows of foreign funds as some flight capital returns, foreign debt is forgiven or rolled over, and the IMF and the World Bank re-engage. Many of the individuals and firms that moved cash overseas in anticipation of the devaluation will gradually bring that money back. Devaluation will make several CFA countries eligible for more Western aid because—at realistic exchange rates—their GDP is now worth less in dollar terms, placing them lower on the ranks of developing nations. [REDACTED]

French and African CFA leaders clearly are concerned—with good reason, in our view—about the potential for the devaluation to trigger political and military unrest that would discourage foreign capital

²Several CFA leaders have cited the serious unrest that resulted from harsh austerity measures adopted in the Central African Republic in 1981 and in Cote d'Ivoire in 1990 as examples of popular backlash against economic policies. [REDACTED]

Faster Overall Economic Growth, But...

We believe that the CFA franc devaluation will contribute to a modest overall improvement in GDP growth performance this year among African CFA economies—dominated by growth in Cote d'Ivoire and Senegal—but at the cost of higher inflation rates and with conditions varying widely among member countries. Moreover, our fairly upbeat regional assessment rests on several assumptions:

- *With IMF and World Bank approval, most of the African CFA governments will make up a portion of the lost real income of public-sector employees and continue the temporary price controls, limiting any political backlash to devaluation.*
- *The CFA countries will receive a net inflow of foreign capital as a result of debt forgiveness, returning flight capital, and new bilateral and multilateral loans and aid.*
- *The CFA governments will pass a large portion of the CFA franc-denominated price increases for export commodities on to producers, while reducing any government subsidies.*
- *Dollar-denominated world-market prices for coffee and cocoa will hold steady or continue to firm.* [REDACTED]

inflows and potentially threaten regime stability or the outlook for democratization in CFA countries.² The groups that stand to lose the most—civil servants, state-owned enterprise employees, unionized workers, and senior military officers—are highly visible and influential because they live in urban areas, are important constituencies for ruling parties, and can protest policies that hurt their relatively privileged lifestyles. Moreover, the devaluation follows austerity measures adopted last year by CFA governments as their finances deteriorated sharply. For example, several governments cut civil service salaries by 10 percent or more in 1993. [REDACTED]

~~Secret~~

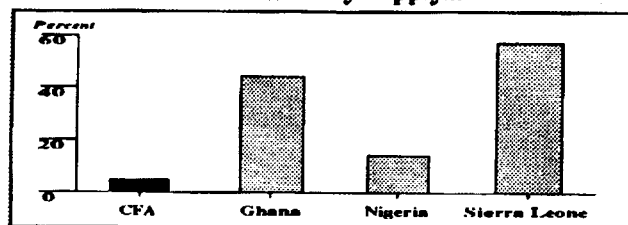
~~Secret~~

POOR QUALITY PAGE

Figure 2

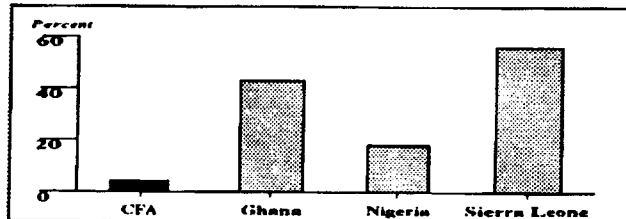
West Africa: Economic Performance of CFA Versus Non-CFA Countries

Better Control Over Money Supply...



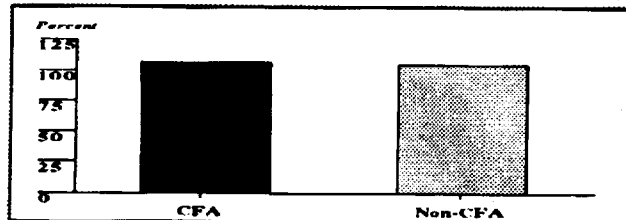
Average Yearly Money
Supply Growth, 1981-90

...Has Helped Rein in CFA Inflation Rates...



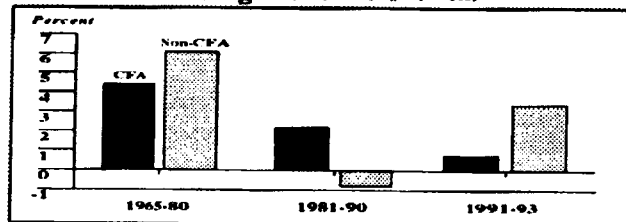
Average Yearly Change in
Consumer Prices, 1981-90

...But CFA Countries Have Done No Better Containing Foreign Debt...



Ratio of Foreign Debt to
GDP, 1991

...Or At Promoting Economic Growth.



Average Yearly GDP
Growth Rates, Adjusted
to Purchasing Power Parity

~~Secret~~

~~Secret~~

Some African CFA countries have already taken steps to insulate key constituencies from the impact of the devaluation and more moves are likely. In particular, several governments have announced plans to partly roll back austerity measures, reverse recent wage cuts, or impose temporary price controls. These steps—combined with widespread popular confusion over the implications of the devaluation and well-publicized offers of donor support—seem to have blunted the initial public reaction. The urban elites so far have generally registered only limited protest against devaluation and earlier austerity measures—warning strikes of one to three days have been common—although some longer strikes have occurred. In our view, many civil servants, parastatal workers, and union leaders are suddenly resentful that, from their perspective, the brunt of austerity has fallen on them. Many probably expect that other changes in import tariffs, export subsidies, and government spending patterns will follow, and some may have adopted a wait-and-see attitude about assessing the overall impact as have ill-paid enlisted men housed in and around capital cities. [REDACTED]

Provided that serious and sustained unrest does not occur and commodity prices continue their recent firming trend, we believe that many of the CFA economies will experience faster GDP growth over the next few years, partly as a result of the devaluation. Academic and IMF economists note that a devaluation could have either a net expansionary or contractionary effect on economic growth in a country, depending on local conditions. In our judgment, for many CFA countries, the dampening effects on imported goods and services of higher prices—which have lowered real income and wealth—will be counterbalanced by foreign capital inflows and a temporary relaxation of government austerity measures. [REDACTED]

The Long-Term Adjustment Faces Risks as Well

In our view, the devaluation represents a significant step toward correcting longstanding foreign and domestic imbalances in the African CFA economies. On the external side, devaluation will speed efforts to cut trade deficits by raising the cost of foreign goods in CFA franc terms and by making CFA exports more competitive. Some local observers have questioned whether the devaluation will boost exports for the small

Sahelian economies and for those countries that sell goods at dollar-denominated prices. We believe that, so long as higher CFA franc prices are passed on to producers, devaluation will raise profitability and encourage increased exports for a wide range of products and countries—but the response may occur only very gradually for some of the African CFA economies. [REDACTED]

Devaluation, in our view, was necessary but not sufficient to correct the domestic imbalances—hefty government spending deficits, inflated civil service salaries, and gutted investment programs for upgrading economic infrastructure and education. To be effective, devaluation must be backed by continued vigilance in maintaining or re-establishing economic austerity and reform. Otherwise, experience elsewhere in developing countries teaches that devaluations can beget rising inflation rates, falling real effective exchange rates, and growing economic pressure for further devaluations. The CFA governments do not have the same latitude as most developing nations to undercut their devaluation through expansionary monetary policy. Nevertheless, efforts to shield the real purchasing power of civil servants and other urban elites through price controls or a relaxation of austerity measures could have similar damaging economic effects—unless these are expedients that last only a few months. [REDACTED]

Implications for the United States

Although the CFA franc devaluation represents a breakthrough in encouraging needed economic growth and reform in Francophone West Africa, it raises the specter that for some CFA countries the gains will be frittered away in efforts to soften its impact or lost to a political backlash. Donors thus face a daunting task of maintaining pressure for further economic reform, while trying to judge the capability of the countries to absorb it. [REDACTED]

Key factors in determining the ability of CFA countries to cope with the impact of devaluation will be budgetary pressures and the extent of recent austerity measures. For example, we believe that Cameroon, Cote d'Ivoire, and Senegal would be particularly vulnerable to popular resistance to any new economic austerity measures because of historically large or well-paid civil services, recent salary cuts, and relatively unionized populations.

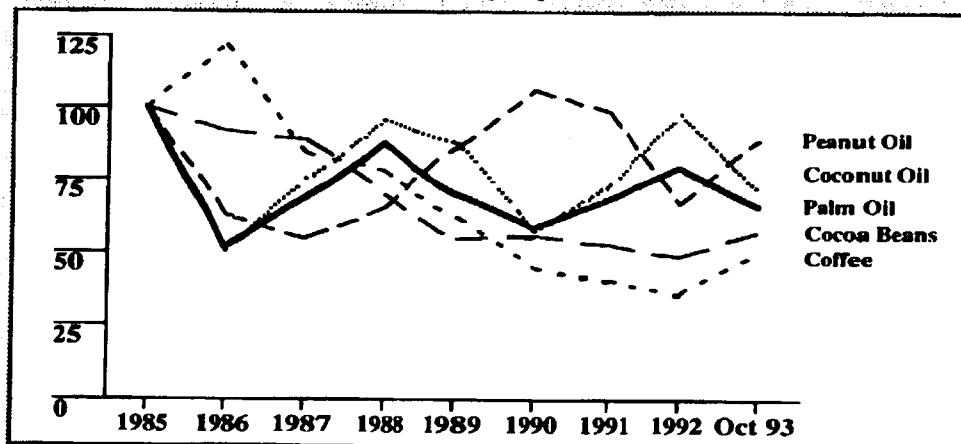
~~Secret~~

~~Secret~~

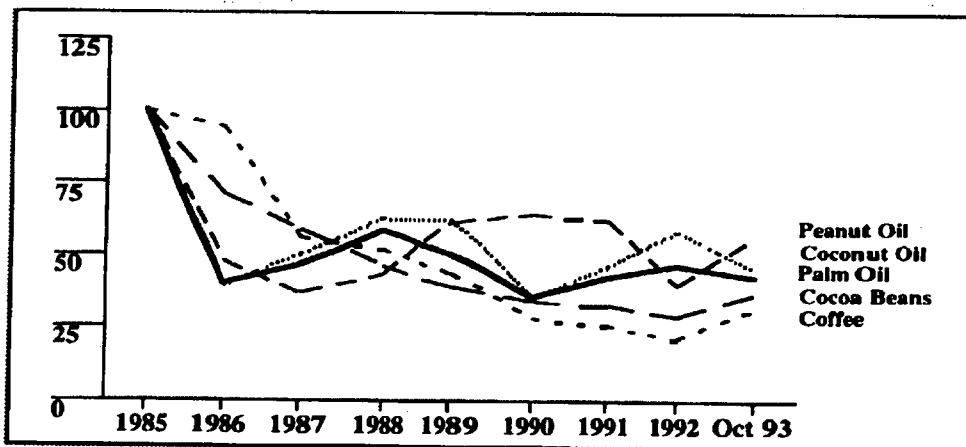
Figure 3

Selected Commodity Price Indices For Goods Sold By Francophone Africa

The CFA Countries Have Faced Falling Export Prices in US Dollar Terms...



...That Have Been Even Worse in CFA Franc Terms Because of an Appreciating French Franc.

~~Secret~~

~~Secret~~

As a result, we do not believe they are prepared politically to make the necessary sacrifices—such as adhering to the terms of new IMF and World Bank conditionality—except under sustained and coordinated urging by the IMF, World Bank, Paris, and Washington. These countries probably will face higher inflation rates than in the past, thus eroding the effects of devaluation somewhat. [REDACTED]

Once the angst over the devaluation has subsided, donors may find some of the CFA governments receptive to follow-on measures designed to increase possibilities for export diversification and foreign investment. Although privatization is politically sensitive in West Africa—and popularly denounced as “selling the national patrimony”—the devaluation of the CFA franc has removed an important impediment to privatizing state-owned enterprises in CFA countries by lowering their likely sales price in foreign currency terms and, for those that export, by improving their profitability.³ In addition, other reforms that improve domestic investment climates, modernize banking sectors, or create export-processing zones are more likely to prove effective now that the price of foreign currency in CFA countries more accurately reflects its scarcity. [REDACTED]

[REDACTED]

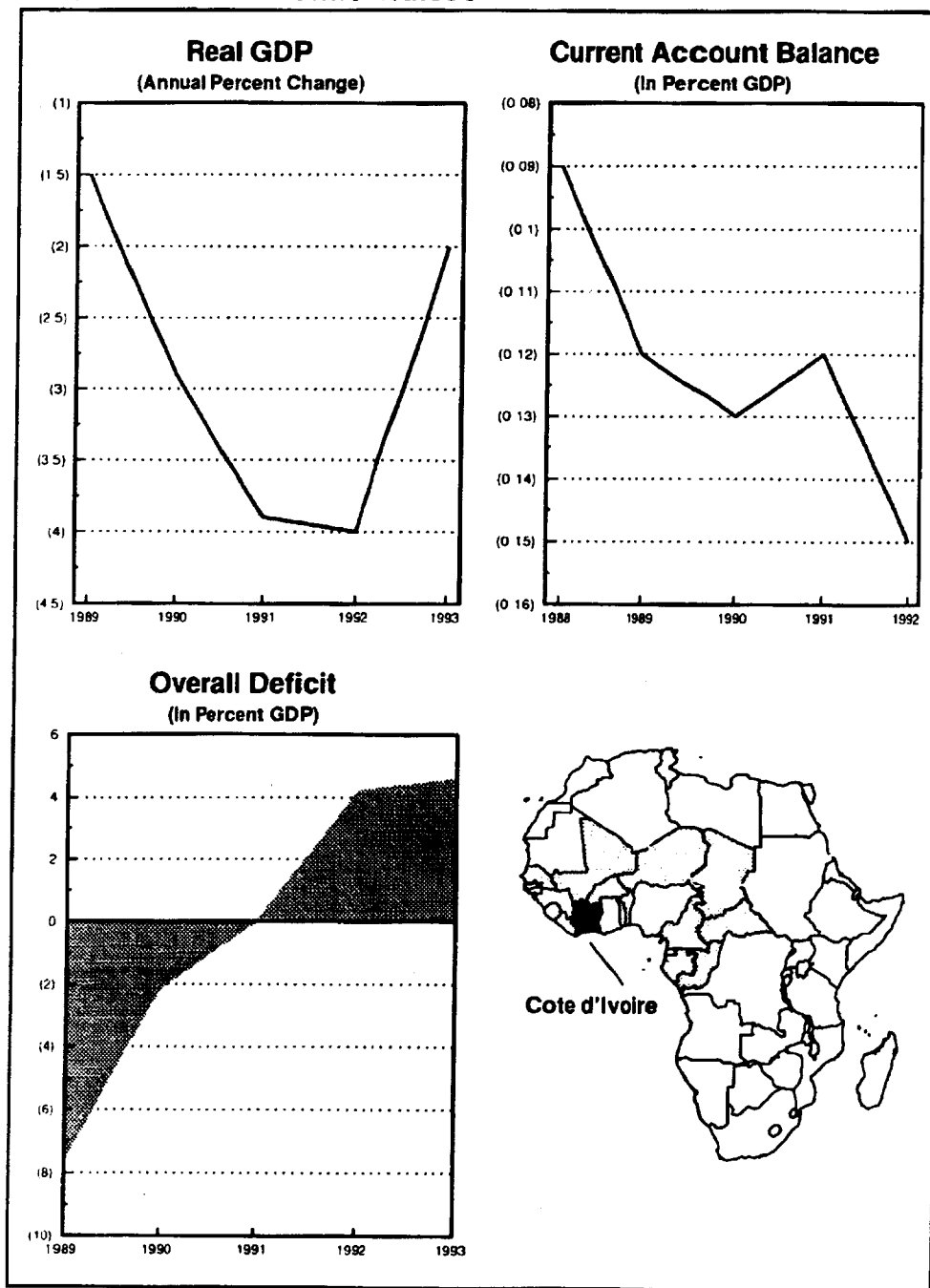
[REDACTED]

~~Secret~~

POOR QUALITY PAGE

~~Secret~~

Cote d'Ivoire: Economic Indices

~~Secret~~

~~Secret~~

Cote d'Ivoire: Facing a Tough Time Selling Devaluation

Following the death of longtime President Houphouet-Boigny, pressure is likely to increase on his untested successor, President Bedie, to give economic concessions to key political constituencies, a situation that could undermine the benefits of devaluation to Abidjan as a major regional labor market and exporter. The country's once prosperous economy slipped into economic decline in the past decade as Houphouet failed to address structural problems and make politically difficult reforms. The economically strapped Ivorian society is likely to react first to the negative consequences of devaluation, potentially sparking urban civil disturbances that could take on antiforeign overtones. Continued assistance and pressure from multilateral and bilateral donors are needed to ensure that Cote d'Ivoire's political vulnerabilities do not undermine the benefits of devaluation and renewed donor support.

Backdrop to Devaluation

Because of the uncertain outlook for world prices of Cote d'Ivoire's principal commodity exports and the economy's continuing competitiveness problem, the Bedie administration faces difficult reform measures with potentially severe political ramifications. Cote d'Ivoire's past unwillingness to change spending patterns—despite falling commodity prices and revenues—led to extensive borrowing to finance budget shortfalls during the 1980s, resulting in a \$20 billion debt. Recently, Ivorian failure to implement politically difficult reforms—such as trimming the civil service and tackling extensive privatization of state enterprises—led to a suspension of IMF and World Bank agreements. Moreover, France—whose financing of Ivorian budget shortfalls has increased yearly to \$500 million in 1993—announced last December that continued budgetary assistance for Francophone states would be tied to satisfactory agreements with the IMF and World Bank in December.

Cote d'Ivoire—undergoing its first presidential transition since independence in 1960—may be more vulnerable than other CFA countries to domestic pressures to slow or reverse economic reforms. Bedie is likely to encounter resistance from key ruling party constituencies if he tries to implement overly painful economic reforms. During Bedie's tenure as National

Leadership and Devaluation

Ivorian leaders are politically vulnerable to devaluation and accompanying reform during the transition period from Houphouet's death to elections scheduled for October 1995.

~~Secret~~

ALA AR 94-002

4 February 1994

~~Secret~~

Assembly President, battles with then Prime Minister Ouattara resulted in the scaling back of many of Ouattara's planned economic reforms, including privatization. Against the backdrop of concern about his leadership abilities, and past corruption charges, Bedie shrewdly appointed close Ouattara associate and former Finance Minister Duncan as Prime Minister, to try to reassure both opponents and donors that Cote d'Ivoire's economic portfolio was in competent hands. [REDACTED]

Trying To Soften the Blow

Better prepared than many of its CFA neighbors to wage a positive public relations campaign, the government immediately went on the offensive. Duncan has announced measures to lessen the impact of devaluation and solicited support from international donors.

[REDACTED] Duncan imposed a three-month price freeze on essential goods, increased producer prices and government salaries, and reduced customs duties. Consumers are being urged to assist the government in cracking down on price control violators by calling a special hotline. [REDACTED]

Reaction from key interest groups has been mixed, reflecting their conflicting agendas. Leaders of the two major groups of labor unions—the opposition-linked independent Confederation of Independent Trade Unions (FESACI) and a ruling party-affiliated General Union of Workers (UGTCL)—are finding that rank-and-file concerns cut across party lines and that common ground may develop as further economic reform measures are announced. [REDACTED] FESACI leaders are demanding an end to the 10-year freeze on civil servant salaries, government payment of salary arrears, and increases in worker salaries commensurate with the devaluation. Wholesalers of pharmaceuticals and fuel are working with relevant government ministries on adjusting price control policies to preserve profit margins and stave off supply shortages. Peasants, farmers, and rural cooperatives—recipients of producer price increases—are adopting a wait-and-see position on the devaluation's impact, but acknowledge that farmers may be inclined to withhold export crops if costs rise too quickly. [REDACTED]

The devaluation has presented Cote d'Ivoire with an unusual opportunity to renegotiate donor assistance, helping the government to cushion devaluation's initial

shock. [REDACTED] Ivorian officials used last month's summit in Dakar to begin negotiations with international financial institutions for renewed assistance. France has canceled 50 percent of Cote d'Ivoire's debt to the Caisse Francaise de Development—approximately 45 billion CFA francs—and expects to inject 660 billion CFA francs, or \$1.1 billion, into the region in 1994. [REDACTED] Cote d'Ivoire's decline in per capita income after the devaluation qualifies it for the most generous terms available from international financial institutions. [REDACTED]

Status of IMF Negotiations

On 25 January, Cote d'Ivoire became the first CFA zone country to sign a letter of intent with the IMF, paving the way for fresh funds to accompany devaluation and facilitating Cote d'Ivoire's external debt negotiations. The new structural adjustment facility, worth \$465 million in 1994, resumes assistance flows suspended in 1992. Moreover, the new agreement and devaluation will facilitate the rescheduling of Cote d'Ivoire's \$20 billion external debt at concessional terms during a 28 February Paris Club meeting. [REDACTED]

Devaluation No Panacea

Abidjan hopes that the devaluation and accompanying reforms will restore positive economic growth benefiting all Ivorians. Duncan has publicly promised that devaluation will increase the competitiveness of the economy, create a solid basis for sustained economic growth, and normalize relations with creditors. The government also hopes the devaluation will help encourage crop diversification and eventual self-sufficiency in food staples, such as rice. [REDACTED]

Average Ivorians, who have watched their standard of living plunge 40 percent in recent years, believe a sharp decline in purchasing power is more likely than the promised benefits. Although public sector employees and students received a surprise payment of late salaries and stipends from the government last month, many believe they are still losing ground. Producers of cocoa and coffee—vital foreign exchange earners—received only modest price increases to encourage improved quality in production but not volume; government officials fear a glut in world production would drive

~~Secret~~

~~Secret~~

prices down, according to Embassy reporting. The devaluation also is likely to cut the incomes of some 300,000 Lebanese traders who depend on the sale of imported goods for their livelihood. [REDACTED]

Potential for Civil Disorder, Antiforeign Violence Mounting

Deepening frustration with worsening economic hardship is increasing the chances for urban violence, which could be directed at non-Ivorians. While initial reaction to the devaluation has been calm, the months after Houphouet's funeral on 7 February will be more telling as further austerity measures are announced and hardship sets in. Key unions, for example, almost certainly will resume strike actions, which were suspended for the mourning period. [REDACTED]

[REDACTED] foreigners—including almost 3 million Burkinabe workers and 22,000 French expatriates—fear they may become targets of economically driven protests, potentially leading to a mass exodus. Violence erupted last November against the Ghanaian community, probably fueled by deteriorating economic conditions and political uncertainty as Houphouet lay near death in Europe. [REDACTED]

[REDACTED] Bedie and Duncan are warning Ivorians against disorder, but probably will feel compelled to offer concessions or reforms in the event of civil unrest. Abidjan erupted in violence in 1990 when less stringent measures were implemented, causing the government to repeal its reforms. Moreover, [REDACTED] the government—widely criticized for its inability to stem the anti-Ghanaian violence—began preparing for widespread unrest in November 1993. [REDACTED]

Implications for the United States

Bedie will probably implement controversial economic reforms only in response to significant pressure from the United States and assurances of debt relief, but such pressure risks triggering both domestic opposition and tensions between Washington and Paris. US

recommendations of greater liberalization within the Ivorian economy, increased competitiveness, and thorough privatization of state enterprises would meet continued resistance within the ruling party, as parastatals represent patronage and money-making opportunities for government officials. Moreover, the Embassy reports that sensitivity to US promotion of privatization and removal of investment and trade barriers, which currently favor French interests, has spurred Paris to interfere on behalf of French businesses in contract bidding procedures in order to ensure French predominance in the Ivorian economy. Both Cote d'Ivoire and France will seek US support within international financial circles for improved debt payment terms for Abidjan, especially to downgrade the country to lower income status. [REDACTED]

(REVERSE BLANK)

~~Secret~~

~~Secret~~

Senegal: Diouf's Risky Turnabout

Long an outspoken opponent of devaluation, President Diouf faces his most difficult political challenge as he seeks to build support for economic reforms that will be painful for important urban groups whose sympathies lay with the political opposition. In our view, Diouf—distrustful of IMF assurances that liberalized trade and exchange rate policies will promote self-sustaining growth—is cooperating thus far because he recognizes that Senegal's overwhelming dependence on external financing and desperate fiscal straits demand immediate action. Although the IMF and World Bank have responded to ensure that aid flows resume within weeks, self-generating economic improvement will remain elusive. Moreover, in the coming months, as the full impact of the devaluation and renewed austerity measures hit the populace, we expect labor groups, students, and politically well-connected businessmen to launch a full court press against policy reform. Diouf has caved in to such pressure in the past, but increased competition for IMF and World Bank aid, diminishing French willingness to subsidize Dakar, and Diouf's concern with posterity as he serves his final term will exert unprecedented pressure on him to go all the way this time—altering the political landscape forever.

Economic Backdrop to Devaluation

Under partially implemented World Bank and IMF structural adjustment programs, Senegal achieved a respectable 3.2 percent annual rate of growth between 1986 and 1992, and by 1990 virtually eliminated its fiscal deficit. While such progress was testament to the improved incentives facing the agricultural sector and Dakar's curtailment of nonwage public spending, it must be measured against a 3.2-percent growth in population, which kept per capita income stagnant, and the budget's heavy—and increasingly formalized—reliance on inflows of foreign aid. This fragile modus vivendi came undone when the IMF suspended lending in mid-1992 following the government's lack of progress in reducing the public sector wage bill and its reversal of several key trade reforms.

The suspension of IMF lending, combined with a deepening trend in declining tax revenues, brought about a fiscal crisis last year, forcing Dakar to implement a 15-percent public sector wage cut in a desperate attempt to win renewed aid. With the failure of this effort and the announcement by France in September that budgetary aid would henceforth be dependent on Dakar's good standing with the IMF, Diouf—who torpedoed past attempts to adjust the overvalued CFA franc—quietly folded his cards and bowed to devaluation.

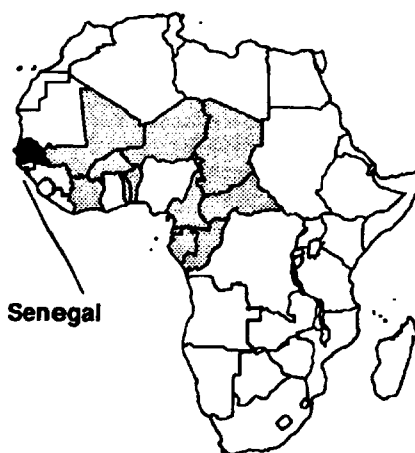
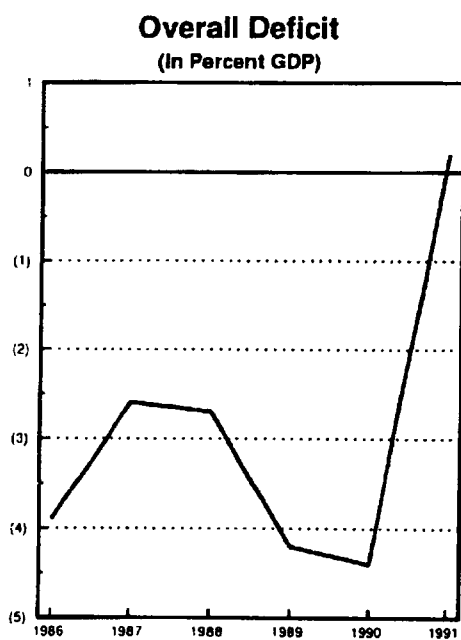
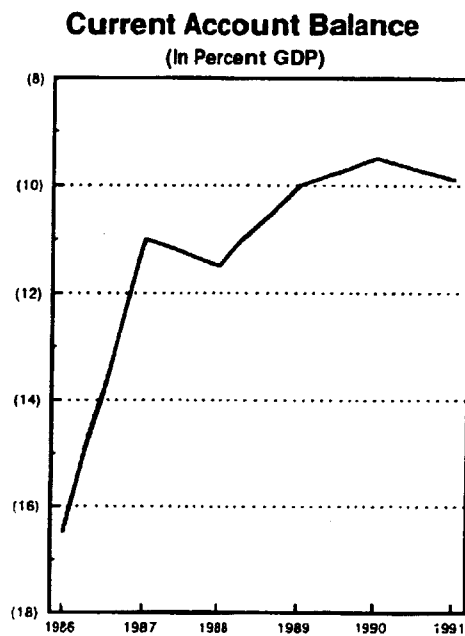
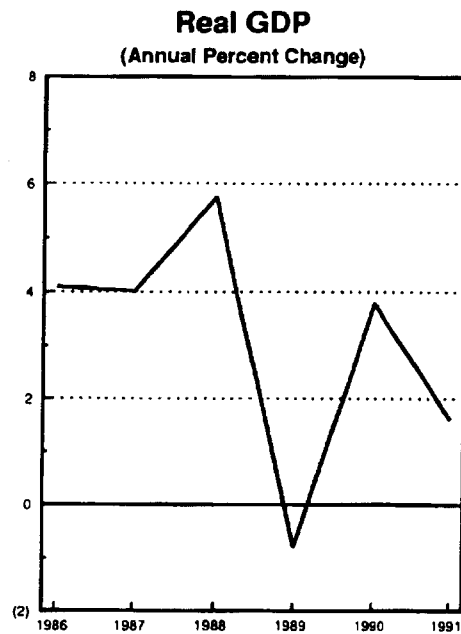
Minimizing the Political Costs for Now

While reaction to the devaluation has thus far been mild, Diouf's about-face has unsettled organized labor and monopolistic business interests. Diouf campaigned for reelection last year, promising to create 20,000 new jobs, preserve employment in the manufacturing sector, and expand markets for Senegalese industries, while rejecting arguments that the CFA franc was overvalued. As recently as September, Diouf ruled out devaluation, promising the nation that wage cuts were sufficient to cure the country's economic ills. Failure to deliver on these promises and to stave off IMF-dictated comprehensive reform has left him vulnerable to charges of mismanagement and betrayal of trade unions and industrial employer associations.

A confluence of political events with the devaluation, however, may eliminate a threat from Diouf's arch political rival, Abdoulaye Wade.

The government plans to try Wade in February for complicity in the assassination of an election judge last May after disputed legislative races. The government case is reportedly strong and Wade's legal counsel has advised him to refrain from public antagonism of Diouf. Wade's party made significant inroads in Dakar and other urban areas in last year's presidential and legislative races, and as recently as October, appeared to be gearing up for a series of protests against Diouf's economic reform package.

~~Secret~~

~~Secret~~**Senegal: Economic Indices**~~Secret~~

~~Secret~~

Wade's uncharacteristically meek criticism of the way devaluation has been handled thus far—notwithstanding his long established advocacy of monetary adjustment—lends support to a preoccupation with legal worries that will give him pause in leading opposition resistance to devaluation. [REDACTED]

A vigorous public relations blitz on devaluation's long-term benefits also has figured in Diouf's ability to escape serious political damage thus far. Diouf, Prime Minister Thiam, and Finance Minister Sakho began meeting with key interest groups, including leaders of the major trade unions, agricultural cooperatives, and the business community, immediately following the announcement of devaluation. Sakho handled the contentious issue of public sector wages adroitly, announcing a 10-percent rollback of the 15-percent cut. Diouf exhorted business leaders to use their enhanced competitiveness to produce for the regional market and asked the agricultural sector to seize the opportunity to move toward self-sufficiency. [REDACTED]

Diouf's assumption of emergency powers also enables him to avoid getting bogged down in dialogue with fractious political opponents and allows him to move swiftly in balancing the often conflicting demands of donors and domestic groups. The administration has free rein for the next six months to impose price controls, adjust taxes and government salaries, and vary budget appropriations by decree without seeking advice and consent from a possibly contrary national assembly. [REDACTED] Dakar has already used these powers to increase prices for rice, petroleum, groundnuts, and cotton, in keeping with an IMF- and World Bank-sanctioned approach that advocates passing on to producers as much as possible the increase in export proceeds in local currency terms. Diouf's enhanced powers also afford him broad discretion in social program spending that will enable him to head off any upsurge of consumer discontent. [REDACTED]

Donors Give Dakar Room to Maneuver. . .

Prompt action by the IMF, World Bank, and France will lead to a dramatic increase in aid flows and reduced debt servicing that will enable Dakar to easily finance its budget deficit. [REDACTED] the IMF and World Bank will provide nearly \$160 million in new loans, and bilateral aid is expected to account for another \$78 million. The remaining \$218 million

financing gap is expected to be covered after Paris Club debt rescheduling and additional bilateral aid. France has already forgiven approximately half of billion dollars in Senegal's official debt and is determined to see Dakar come before the Paris Club for additional debt relief at the earliest possible date, possibly in late February. [REDACTED]

. . . But Balance of Payments Will Remain Precarious

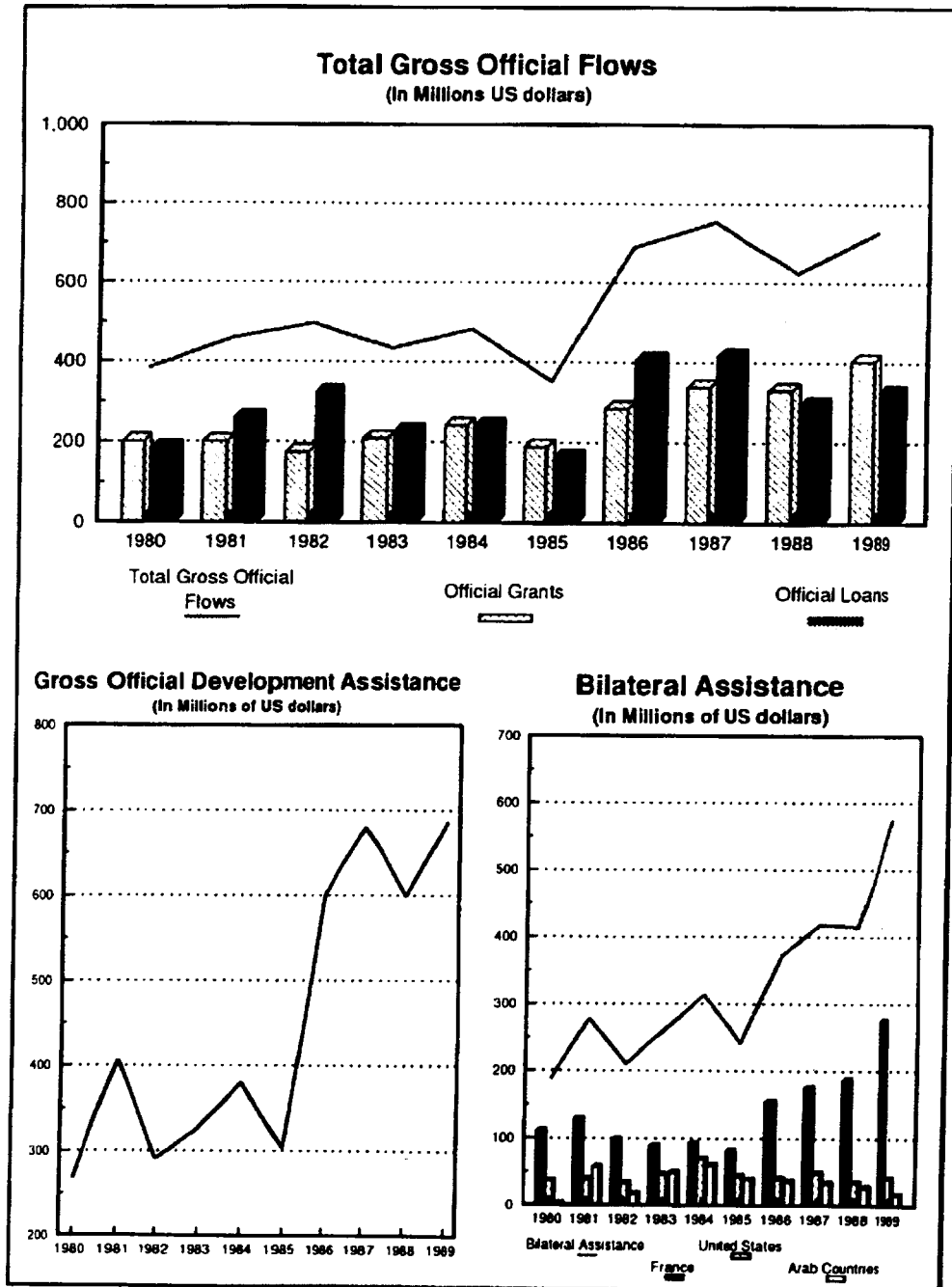
While net capital inflows will dramatically improve as a result of strong donor support, self-sustaining improvement in Senegal's balance of payments will still be elusive because of a number of uncontrollable factors and structural constraints affecting the current account. Forecasts for growth in the export sector, including groundnuts, phosphates, and commercial fishing are modest even when increased local currency earnings for producers are taken into account. Erratic rainfall, a drop in cultivated acreage, decreasing cash crop production, and falling world prices plague groundnuts, Senegal's mainstay hard currency export. Near-term prospects for increased fish exports, the leading source of foreign exchange in recent years, are likewise poor, in view of the exhaustion of fisheries, high processing costs, increased competition from Southeast Asian countries, and tightening quality controls in European markets. The phosphate industry faces growing international competition and fewer markets for this environmentally unsafe product. As a result, hard currency earnings—and consequently government revenues derived from exports—are unlikely to increase substantially in the near term. [REDACTED]

Imports also will remain problematic in the short term. The modest improvement in the trade balance over the past several years can be attributed to already diminishing import demand in consumer and capital goods categories, as well as dramatic reductions in world prices of rice and petroleum. Imports of food, beverage, and tobacco, however, recorded strong growth. As a result, in the short term, under price controls and subsidies for food imports, and because of entrenched taste preferences of politically influential urban elites, the value of imports is unlikely to significantly fall. Indeed, donor-mandated increases in investment will probably fuel growth in capital goods imports and the value of petroleum imports could rise again if world prices emerge from their current slump. (C NF)

~~Secret~~

~~Secret~~

Senegal: Official Resource Flows

~~Secret~~

~~Secret~~

Mounting Political Risks

Although Diouf has easily handled the immediate aftermath of devaluation, we believe he will face much greater challenges in the coming months as the populace absorbs the full impact of devaluation and urban interest groups feel the bite of other reform measures. In particular, the lifting of price controls and the elimination of subsidies will spark sporadic labor and student demonstrations and strikes. The resumption of trade and labor reforms that are critical to Dakar's ability to take advantage of devaluation almost certainly will lead to labor unrest because they entail layoffs of thousands of excess workers and closing of inefficient firms. While Diouf may be tempted to stall on these fundamental changes as he did throughout the late 1980s, we believe greater donor pressures will compel him to follow through despite the political risks. On balance, Diouf will weather these difficulties, but he will see a further decline in his popularity. [REDACTED]

Although the public will step up the rhetoric and interest groups will noisily take to the streets during periods of economic unrest, we do not expect that the regime will be seriously threatened because it can count on the loyalty of traditionally apolitical security forces. Police and gendarmerie units are well versed in restoring order, and Diouf will call on the military only as a last resort. [REDACTED]

Implications for the United States

The Diouf administration, after years of muddling through on economic reform, almost certainly will grouse in private about tougher conditionality, but we believe Diouf's concern for Senegal's international prestige will prevent him from scapegoating Washington. [REDACTED] Diouf remains highly skeptical that private investment—especially from the United States—will be drawn to Senegal under a more liberalized economy. Adding to his worries, increasing urbanization and unemployment among city youth play into the hands of radical Islamic activists—still a minority—who are ideologically opposed to Western-style capitalism. Traditional Muslim leaders, long allied with the ruling party and who command the rural vote, will oppose attempts to bring the lucrative underground economy into a formal

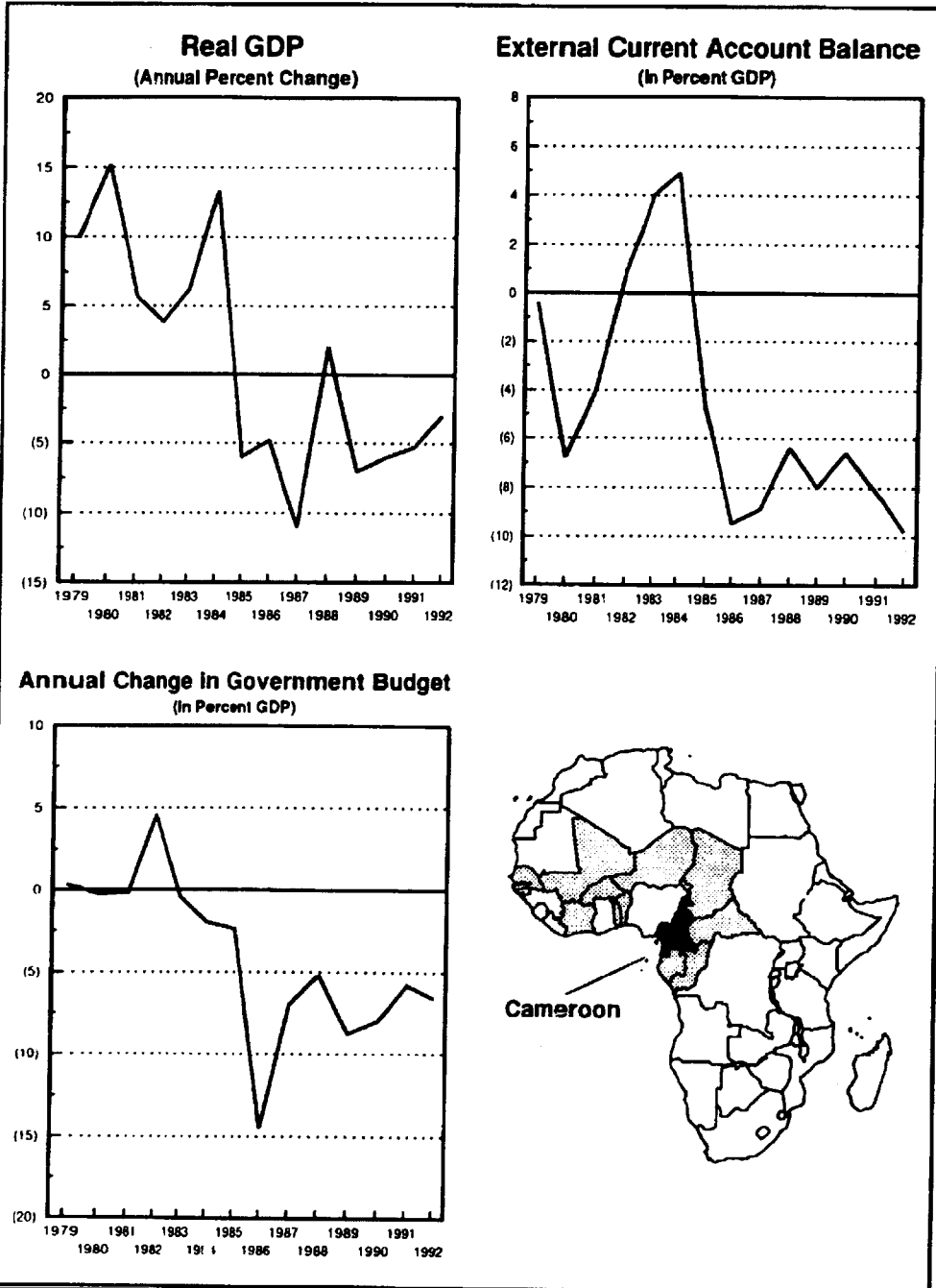
accounting. As a result, Diouf will face a bewildering chorus of calls from business elites, labor and student leaders, and Islamic figures to resist the IMF-prescribed solutions. [REDACTED]

Washington and other Western capitals have potentially greater influence over Senegal compared to other more prosperous Francophone countries because of its relatively greater dependence on foreign aid and because of Diouf's determination to preserve the respect long accorded Senegal as a model African multiparty state. Diouf has garnered considerable favor—often translated into increased bilateral aid—for Senegal through the years through his constructive participation in international forums such as the Organization of African Unity and the Islamic Conference Organization. He probably recognizes that if Dakar is to maintain its favored standing among the crowded field of international aid supplicants, he will be wise to parley donor demands into the type of politically empowering economic reform that ensures continued support from the West. By enlarging political participation to directly include those groups—rural education and health-care leaders, small- to medium-scale businessmen, and the entrepreneurs of the informal economy—Diouf can reshape the balance of political power in Senegal. [REDACTED]

~~Secret~~

~~Secret~~

Cameroon: Economic Indices

~~Secret~~

~~Secret~~

Cameroon: Government Ill-Prepared To Take Advantage of Devaluation

Of the CFA franc zone's larger economies, Cameroon is probably the least equipped politically and economically to take advantage of the potential benefits of devaluation to halt its economic slide. The CFA devaluation came soon after a draconian cut in public sector wages that has sharply curtailed Cameroonians' earning power and increased popular discontent. Without an infusion of international aid to cushion the immediate effects of the devaluation, shortages of consumer goods and worsening living conditions—especially in urban areas—are likely to trigger civil unrest. Nonetheless, President Biya may decide not to implement preconditions set by the IMF for a standby agreement out of fear that increased financial accountability will lead to exposure of past misdeeds and prevent him from continuing to buy off critical political allies. Biya is likely to stall on implementing austerity measures, but he will probably expect creditors to follow France's lead in extending debt forgiveness and to pressure the World Bank and the IMF to ease up on calls for reform that could provoke a political backlash.

Backdrop to Devaluation

Cameroon's economy, heavily dependent on oil exports and, to a lesser extent, on coffee and cocoa, began a steady contraction with the decline in oil, coffee, and cocoa prices in the mid-1980s. The deterioration was hastened by mismanagement and misuse of government revenues. In 1991 opposition party leaders, seeking to exploit popular discontent over the decline, launched "Operation Ghost Towns," which shut down all business and commercial activities for days at a stretch, worsened the economic crunch, and alarmed the economically significant French business community.¹ Last year Yaounde for the first time was unable to meet its bloated

¹The French own some 150 firms in Cameroon, including half of all foreign-owned companies in the agroindustrial and manufacturing industries. Bilateral trade—consisting mostly of Cameroonian oil exports to France—totaled some \$1.4 billion in recent years, and in 1990 Cameroon was France's leading trading partner in Sub-Saharan Africa. Cameroon also sits astride land routes to Chad and Central African Republic, areas where Paris has significant security interests. France is Cameroon's leading source of security assistance, providing about 60 military advisers, 20 military doctors, and an additional \$3 million in grant aid.

civil servant payroll on time. Under pressure from France and international financial institutions and with no other options, the government imposed up to 50-percent cuts in civil servants' salaries and a 30-percent cut in military pay, precipitating a general labor strike that continues to disrupt all sections of the economy.

Yaounde has refused to negotiate with the workers—who are demanding payment of salary arrears for last September and October, a review of last November's pay cuts, and reinstatement of workers suspended for strike-related activities—and instead has attempted to bully them into returning to their jobs.

On the political front, Biya faces stiff opposition from opponents who continue to protest his victory in the fraudulent presidential election in October 1992. The President's blatant favoritism toward his Francophone Beti tribe and heavyhanded tactics against his main rival, the English-speaking Social Democratic Front led by John Fru Ndi, are further fueling political and ethnic tensions. Moreover, anti-French sentiment among many Cameroonians is worsening because Paris—the former colonial power and main source of external assistance—is seen as backing Biya against the opposition and interfering in the country's internal affairs.

Counterproductive Government Moves Heighten Tensions

The government's initial actions in response to devaluation so far have been marked by confusion and a lack of coordination. Biya, who normally keeps a low profile in day-to-day government operations, agreed in late January to chair the newly created National Economic Affairs Committee charged with formulating Yaounde's post-devaluation economic policies, but he is now in Europe for medical treatments, complicating the government's ability to quickly implement sound policies. Under pressure from merchants, Yaounde allowed steep price increases on some essential goods, including sugar, flour, bread, and

~~Secret~~

~~Secret~~

pharmaceuticals, but then mitigated their effects by instituting price controls for a six-month period. [redacted] price controls have already begun to produce shortages. Flour, for example, is largely imported, and is becoming more expensive. Government inspectors have closed bakeries that have refused to comply with price controls, prompting others to close voluntarily rather than sell at artificially low prices. [redacted]

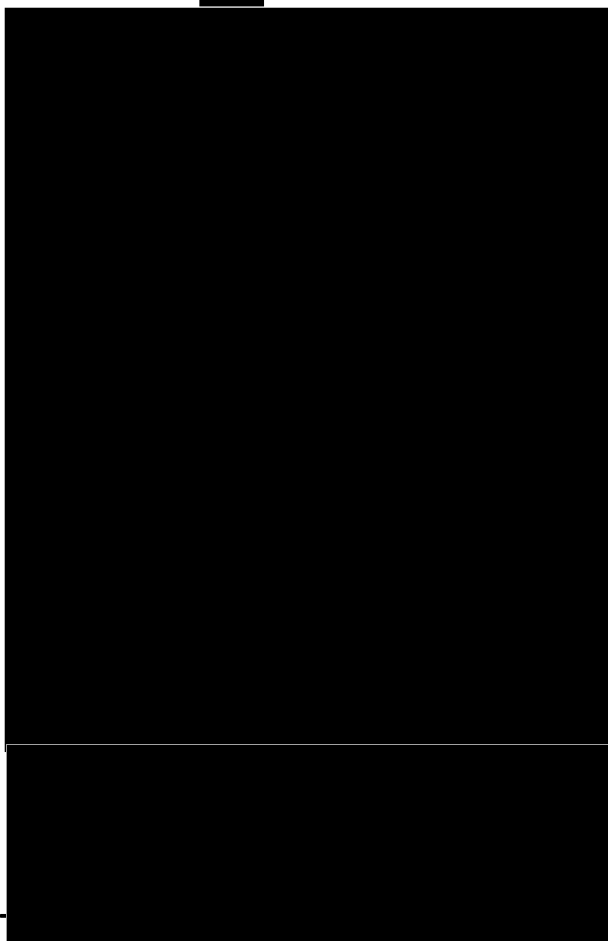
The business community, opposition political groups, and some government officials welcome the devaluation. They believe it will force the regime to adopt long-needed reform measures that will benefit the economy—especially the agricultural sector—in the long term. The public at large, however, appears skeptical. The overvalued franc had subsidized an urban elite of manufacturing workers and public sector employees who now face loss of their privileged positions and cheap access to imported goods. The Embassy reports that urban workers are demanding tighter price controls and salary increases, and Yaounde's refusal to negotiate is making the formerly passive labor movement more militant. [redacted]

France last week announced forgiveness of 50 percent of Cameroon's bilateral debt, but Paris has finally joined the rest of the international community in pressing Yaounde to undertake serious financial reforms. [redacted]

[redacted] French debt relief included forgiveness of all arrears, clearing the way for Paris to begin new assistance programs that may help cushion the social costs of the devaluation. Nonetheless, Paris will not resume direct budgetary assistance, discontinued last December, until Yaounde has an IMF program in place that signals its willingness to institute economic reforms. [redacted]

The Bretton Woods institutions remain skeptical about Yaounde's commitment to economic reform and are requiring improved financial performance before considering even a standby facility [redacted] Before the letter of intent for a standby agreement can be delivered to the IMF in Washington, Yaounde must produce a plan for cutting the government payroll further, phasing out price controls, and lowering import tariffs. It must also improve accounting for the state oil company and draw up a

more realistic—and more transparent—budget. To mitigate the immediate effects of the devaluation, the IMF reportedly is considering releasing the final \$50 million tranche of an existing loan package that has been delayed by Yaounde's failure to meet performance goals. Nonetheless, without a new standby agreement, Cameroon will not be eligible for rescheduling Paris Club debt, which rose to 1,400 billion CFA francs at the new conversion rate. [redacted]

~~Secret~~

~~Secret~~

A Delicate Balancing Act

Biya has been reluctant to undertake IMF- and World Bank-mandated reforms—particularly severe government wage and employment reductions—for fear of provoking a political backlash from the Yaounde-based civil servants that provide much of his political support. So far, the government has implemented few relief measures, although it has promised tax reductions on essential goods, an adjustment to the price of petroleum products, and a gradual increase of nominal salaries for public sector employees. As a result, tensions remain high, and [REDACTED] relatively minor increases in such items as taxi fares or school fees or prolonged shortages of consumer goods could trigger major riots in the capital. [REDACTED]

The strongest reaction to the devaluation is likely to come from within Biya's inner circle in the short term, and is more likely to focus on the political costs to regime officials of IMF-mandated reforms than on the social costs of devaluation. Senior officials in the government have strengthened their political positions by dispensing patronage and financial incentives, and lax financial accounting has encouraged corruption. Exposure of their malfeasance could lead to reduction in their power or loss of their positions; some officials probably will threaten to implicate Biya in an effort to avoid exposure and hold onto their perquisites. [REDACTED]

Yaounde clearly faces a serious, and potentially regime-threatening dilemma, and Biya is likely to avoid taking any tough decisions. If politicians succeed in blocking further reforms—as seems likely—no new IMF agreement will be implemented and devaluation is likely to presage high inflation and increasing hardship. Moreover, the government will remain unable to end the labor unrest without a standby agreement because it lacks the funds to meet workers' key demand—payment of salary arrears—and urban tensions will continue to rise. At the same time, however, implementing an IMF plan involving transparency in government is likely to lead to scandalous revelations that, fanned by opposition rhetoric, are likely to provoke outbreaks of anti-government violence. Worsening Biya's worries, some elements of the military may be unwilling to move against their own citizens to restore order or to refrain from economic-based protests of their own. [REDACTED]

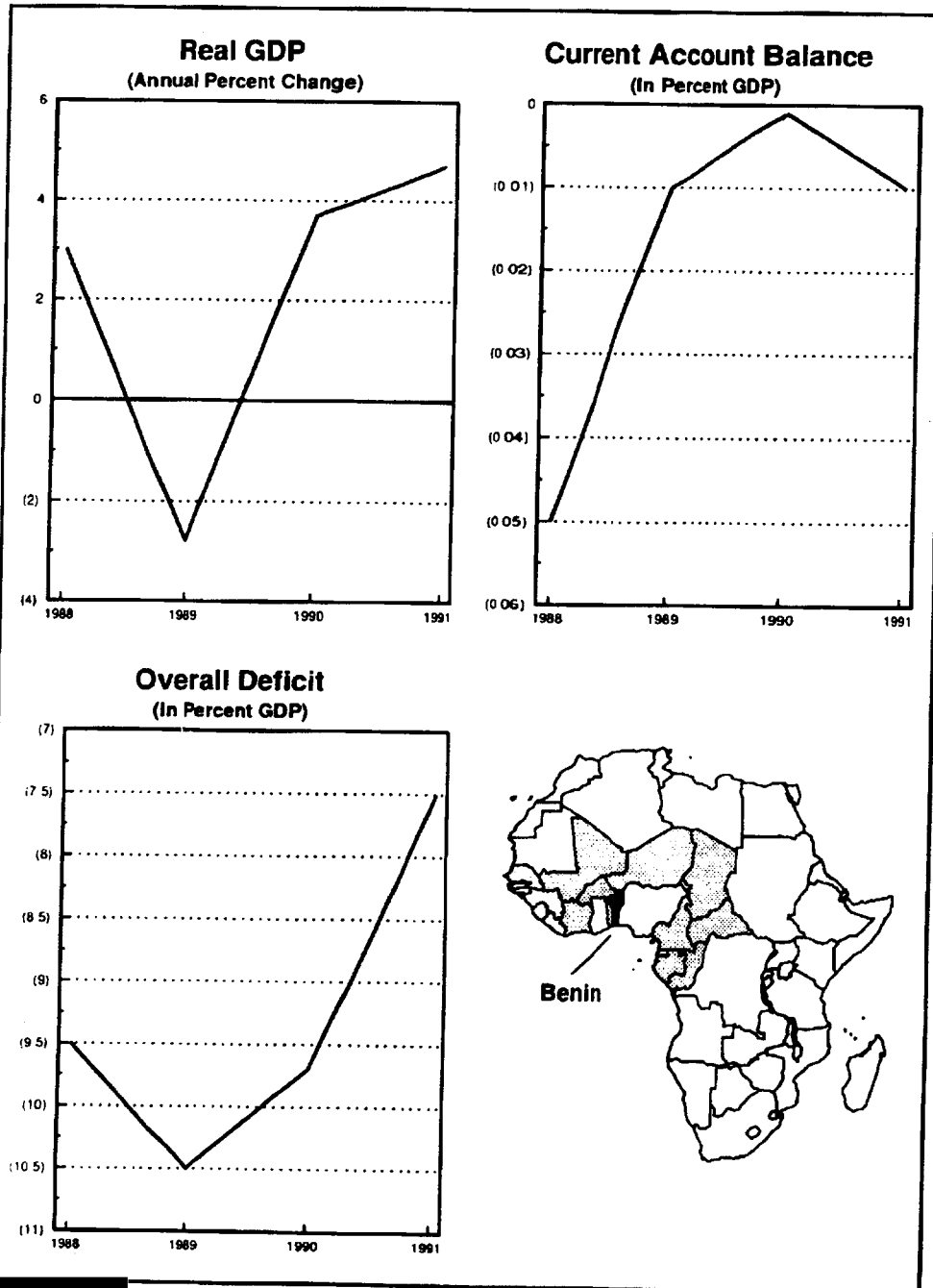
Regime officials have begun to seriously discuss the possibility of withdrawing from the franc zone if Yaounde does not soon secure a new IMF program. They probably hope to use the threat to secure more concessions from the international community. [REDACTED] the regime has already taken some steps to prepare for instituting a national currency, including ordering printing equipment and an initial supply of new notes. Some Cameroonian officials reportedly contend that severing the monetary link to France would increase their independence from Paris and discourage rampant capital flight, since the new currency would lack the convertibility of the CFA franc. Such a move, however, could easily lead to hyperinflation because any Cameroonian central banking structure would be susceptible to pressures from the cash-starved executive to increase the money supply by printing more bills. [REDACTED]

Implications for the United States

US relations with Cameroon, already strained by Washington's criticism of the regime's lack of enthusiasm for democratic reform, probably will further deteriorate if the IMF does not soon approve Yaounde's standby agreement. Believing that the United States wields a disproportionate influence on the decisions of the IMF, Yaounde almost certainly would ignore its own poor reform record and blame delays in reaching a standby agreement on Washington's lack of support. The lack of new bilateral aid or investment from US sources will be seen as further evidence that Washington opposes the Biya regime. [REDACTED]

Economic liberalization—if it occurs—could create opportunities for US firms, both for investment in export-oriented and import-competing production. Cameroon has a relatively well-educated work force and vast underutilized agricultural and energy resources. Imports of US goods, which totalled \$57 million in 1992, are likely to decrease in the near term, while exports to the US—\$83 million in 1992—may increase as they become more competitive. Cameroon hopes for new Western investment in the oil sector and in potentially lucrative agricultural products, such as bananas, in the wake of the devaluation. [REDACTED]

~~Secret~~

~~Secret~~**Benin: Economic Indices**~~Secret~~

~~Secret~~

Benin: Putting Fragile Democracy to the Test

President Soglo's determined pursuit of economic reform has been rewarded with three straight years of economic growth, and he is likely to press forward with reforms despite the potential political backlash caused by the CFA devaluation. His political support in the parliament is already eroding, however, and he faces an uphill battle in maintaining a governing consensus and consolidating his authority. A French-trained economist, Soglo has long supported the need for devaluation, but he will need to act quickly to calm public fears and build support for continued austerity. Although labor and student groups are likely to renew demands for salary hikes and other economic relief, we believe the government will be able to prevent significant unrest, unless the military's lower ranks become seriously restive.

High Hopes for Economic and Political Turnaround
Benin's underdeveloped economy has improved steadily since the country's transition to democracy in 1991. The government has privatized over 70 state-owned enterprises and reduced inflation to approximately 2 percent. Government wages have been frozen at 1986 levels in accordance with the IMF structural adjustment program, and the country's GDP has grown for three years in a row. Nevertheless, Benin's limited resource base and the vulnerability of its major export—cotton—to fluctuating world prices continue to constrain its economic potential. In addition, the government has had difficulty managing relations with powerful labor and student groups, who often resort to strikes and protests when their unrealistic wage and scholarship demands are not met. The commitment of northerners in the military to democratic government dominated by southerners also is questionable. A northern-led coup attempt failed in August 1992.

Soglo's election in April 1991 capped a peaceful democratic transition, but his support in the National Assembly has eroded since then and he faces an increasingly discontented public weary of economic austerity. Soglo's decision to shuffle his Cabinet last September—he replaced some ministers from his party with those from

the opposition—angered many of his key allies in the Parliament and ultimately caused the collapse of his presidential majority there. Growing political opposition in the parliament has delayed passage of the budget and other essential legislation. In addition, Soglo's selection of fellow southerners for government positions—many from his Fon ethnic group—has fueled traditional ethnic and regional rivalries.

Government Ill-Prepared for Devaluation

Despite Soglo's support for devaluation, the government was ill-prepared and slow to respond to the public's initial panicked reaction to the move. The Council of Ministers announced price controls for basic foods and plans to deploy teams of price checkers to ensure the controls are being respected. The government has agreed in principle to raise workers salaries a "reasonable" amount and to create a social fund to help the hardest hit urban areas. The belated announcements have done little to reassure the public or restore order to the marketplace. Many merchants remain closed, while others continue to impose erratic price hikes.

Labor unions and student groups have denounced the devaluation and called for increases in their salaries and scholarship subsidies. The eight largest unions have set up a crisis committee and the president of the Chamber of Commerce announced that his members would refuse to observe price controls. Labor leaders boycotted a session with Soglo after the government banned a union meeting on the devaluation issue.

Unionists have accused the government of violating their rights and warned that such actions are dangerous for democracy.

Soglo has announced that the IMF has offered an enhanced structural adjustment facility and that France intends to cancel Benin's outstanding developmental loans. Senior officials have expressed concern, however, about the lack of expertise among all but the top levels at the Finance Ministry. They reportedly were dismayed by the Ministry's lack of advanced preparation for the

~~Secret~~

~~Secret~~

devaluation and fear it risks being perceived by the public as a lack of direction. Moreover, Soglo's tendency to talk in macroeconomic terms and theories has often confused his colleagues. [REDACTED] and hampers his ability to build public support to sustain reform efforts. [REDACTED]

A Delicate Balancing Act

The devaluation raises the stakes for Soglo's government while he is still struggling to consolidate the country's modest economic gains and new democracy. Soglo's strong record on structural adjustment will open up additional financing from the IMF and World Bank, but he will have to balance the country's long-term investment requirements with the need to cushion the immediate impact of the devaluation. Although he has emphasized that farmers should benefit immediately from increased local currency prices for their products, Benin's weak manufacturing sector and limited export base are unlikely to experience significant growth in the short term. Nevertheless, Benin's low inflation rate and disciplined control of import demand should help it maintain a favorable balance of payments. [REDACTED]

In the short term, Benin is expecting the devaluation to ease government budget pressures. The government calculates that revenues from tariffs will rise in CFA franc terms, although they may decline in French franc terms because of a drop in the volume of imports and reexports to neighboring Nigeria, the region's largest economy. Meanwhile, the devaluation will raise the CFA franc value of cotton exports and the value-added tax. [REDACTED] Public sector wages and other government expenditures are expected to rise less rapidly. [REDACTED]

The government's shaky reaction to the devaluation has heightened public fears, and Soglo will need to act quickly to overcome potential opposition and build a strong case for continued austerity. [REDACTED]

[REDACTED] senior officials are worried that the 50-percent devaluation will so depress purchasing power that it will cause labor unions and other key urban groups to mobilize against the government. Economic-based unrest by the military's lower ranks is also possible. Although temporary price controls should ease the immediate impact of the devaluation, officials are concerned that lifting them would reignite public anger

and undermine the government's position in general elections next year. Continuing price controls indefinitely, however, risks creating major shortages or forcing expensive government subsidies. [REDACTED]

Pursuing Reform Despite the Risks

Soglo, who was elected after labor and student protests brought down the previous regime, is keenly aware of the power those groups wield and almost certainly will try to appease their demands when possible. He remains committed, however, to economic reform and is unlikely to give in to demands that could seriously undermine the reform program. Although Soglo is counting on the promised salary hikes to ease the potential backlash from labor unions and student groups, sporadic strikes and civil unrest are likely as the full impact of devaluation and other austerity measures are absorbed by the populace. Such unrest will not threaten the regime unless key military elements join in, but it will complicate Soglo's ability to govern and to consolidate his own political position. [REDACTED]

Implications for the United States

Although the United States has little strategic or economic interest in Benin, its democratic transition has been held up as a model for West Africa and its ability to cope with the devaluation will be closely observed by other struggling states. Soglo's continued success in carrying out both political and economic reform will be monitored by other leaders, many of whom have argued that such simultaneous reforms place too much stress on society. Soglo, whose record of fiscal responsibility in the face of daunting economic hardships has won respect in the international financial community, clearly wants his efforts rewarded and will probably call for the United States to support new aid and investment. [REDACTED]

The devaluation is likely to force Soglo to focus more on domestic issues, leaving him little time for his duties as chairman of the Economic Community of West African States (ECOWAS). Soglo reluctantly accepted a second ECOWAS term—due to end in July—and has often expressed frustration with the demands it places on his time, particularly because of ECOWAS's effort to mediate an end to the crisis in Liberia. [REDACTED]

~~Secret~~

~~Secret~~

Gabon: Devaluation Likely To Have Few Benefits

With one of Sub-Saharan Africa's strongest economies, Gabon is unlikely to benefit much economically from the CFA devaluation, but it will face many of the same political risks as its franc zone neighbors. President Bongo is the most vocal opponent of devaluation, arguing—with some justification, in our view—that Gabon's oil-dominated economy will be disproportionately harmed by devaluation. He also believes that the economic impact will exacerbate political tensions that are already high following the contentious presidential election in December. While initial public reaction has been muted, the CFA devaluation has slashed the population's purchasing power, and this could spur labor and civil unrest. Over the longer term, manganese, uranium, and timber production may grow, but prospects are poor that the devaluation will stimulate Gabon's oil-dependent economy to diversify, particularly since the outlook for obtaining necessary international financial assistance is dim. Bongo blames the United States in part for the devaluation, and bilateral relations—already strained by Washington's criticism of his harassment of the opposition following the election—could deteriorate further.

Bongo: "We Don't Need Devaluation"

Bongo views the devaluation as unnecessary because Gabon is the only country in the zone where the CFA was not significantly overvalued. Libreville's strong oil-export driven economy has consistently produced substantial trade surpluses—more than \$1.3 billion in 1992. Gabon has averaged around 5 percent annual GDP growth since 1989, and enjoys one of Africa's highest standards of living, with a per capita income over \$5,500.

On the political front, the devaluation occurred at a difficult time because of continuing tensions over the contentious presidential election, which Bongo claims to have won with just over 51 percent of the vote. While fraud was carried out by both sides and Bongo shamelessly exploited all the advantages of incumbency, US election observers believe the vote

generally reflected the will of the people.

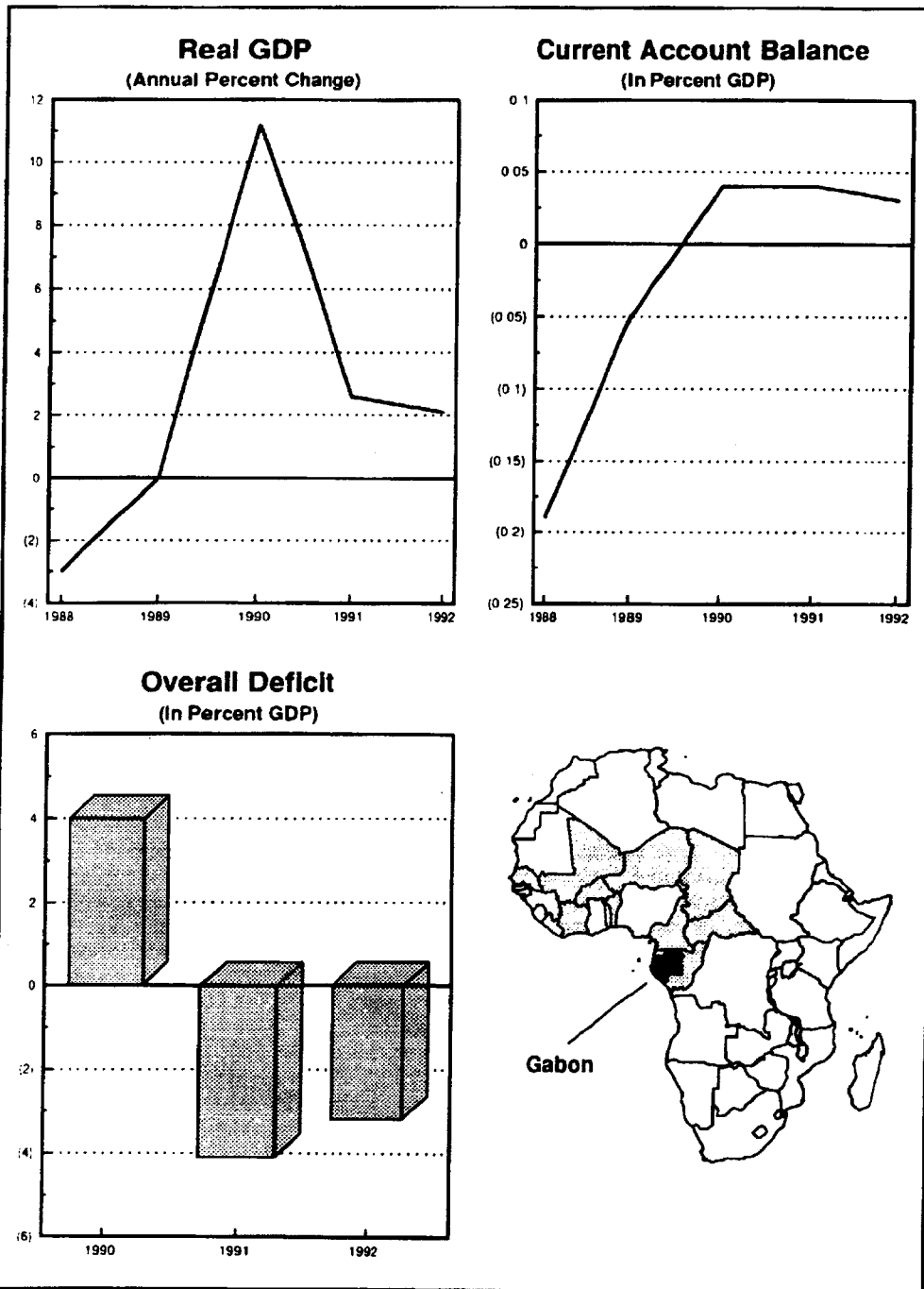
The opposition, however, still refuses to accept the results. It has mounted a persistent campaign to try to have the election overturned and has threatened to form a parallel government. The Bongo government has responded by jamming the opposition's radiobroadcasts, damaging its newspaper facilities, and temporarily barring its leaders from leaving the country.

Initial Reactions Muted

Gabon's initial official reaction—like that of many of its neighbors—was to take steps to limit the impact of devaluation on the people. Prices of essential goods have been frozen until the government decides on a new pricing scheme, and tariffs on imported goods will still be applied at their predevaluation price. Prices continue to increase 50 to 100 percent, however, and many stores are not replacing stock or are closing their doors. Bongo established a government commission to seek financial assistance from the international financial community and to educate the population on the impact of devaluation. The commission will explore establishing a new wage policy, changing the commercial tax code, and amending the government's budget. Media closely linked to Bongo's ruling party are suggesting that Gabon should break with its fellow CFA countries and establish an independent currency.

Popular reactions have been low-key so far despite the devaluation's almost immediate negative impact on all key political sectors. average Gabonese resent being treated like their poorer neighbors in the franc zone, especially because they do not believe devaluation will bring economic improvements. Urban dwellers—nearly 50 percent of the population live in Gabon's three main cities—saw prices of virtually all household goods double or the goods themselves disappear from store shelves. The usual devaluation winners in other CFA countries—farmers, businessmen, and industrial producers—do not exist in large numbers in Gabon, denying the

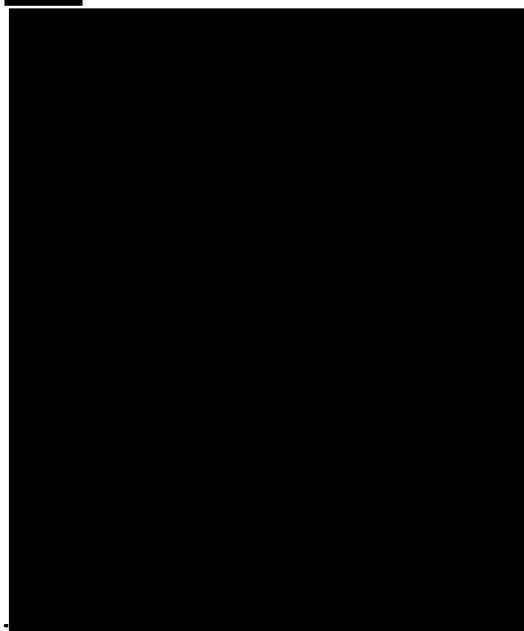
~~Secret~~

~~Secret~~**Gabon: Economic Indices**~~Secret~~

~~Secret~~

government a potential source of political support for devaluation. [REDACTED]

[REDACTED] in recent weeks Bongo has significantly increased his public praise and patronage toward the armed forces, suggesting he may be concerned over their response. The political opposition is charging that Bongo failed to anticipate the impact of devaluation, but is not calling for civil or labor protests. [REDACTED]



Gabon's relative wealth probably rules out obtaining significant Western financial assistance. The IMF says that Gabon does not qualify for its planned program of support to other CFA countries, and the World Bank is unlikely to move independently of the Fund. [REDACTED]

[REDACTED] In addition, Gabon has a poor credit history with international donors. Its Paris Club agreement was suspended in October 1992 and its credit arrears are nearly 30 percent of GDP. France, which has a significant stake in Gabon, recently forgave half of its bilateral debt, but Paris appears unwilling to provide additional financial support, given the need of other zone members.¹ [REDACTED]

¹Over 12,000 French nationals live in Gabon. France provides over 50 percent of Gabon's imports, and Gabon serves as France's primary strategic oil reserve. [REDACTED]

[REDACTED] many French residents in Gabon have seen their livelihoods hurt severely by devaluation and many are planning to leave. Some of Gabon's larger stores are abandoning expensive French suppliers for South African firms, which enjoy significantly less expensive transport costs. Paris may increase its political support for Bongo, however; French officials recently agreed to Bongo's request that they not meet with Gabonese opposition leaders protesting the recent election. [REDACTED]

Devaluation Promises Little Economic Gain

The devaluation will pay few dividends to Gabon's oil-dependent economy, while the short-term hardship it produces might spark some unrest. Gabon's exports, which account for more than 60 percent of its GDP, will at best increase only gradually in response to the devaluation. The country's exports—oil, manganese, and uranium—are priced in dollars and sold at prices determined on the world commodity market, significantly limiting the devaluation's impact on the competitiveness of these products. Gabon has few of the nontraditional or value-added export sectors—manufacturing comprises less than 9 percent of GDP—that typically benefit most from devaluation. The Gabonese have historically lacked an agricultural, trading, or entrepreneurial tradition, gravitating instead toward finance and civil service. Only 0.5 percent of Gabon's land is under cultivation and the dense equatorial rain forest that covers most of the country severely limits suitable land for animal husbandry. Manufacturing sectors that do exist—such as the CFG plywood factory, at one time the world's largest—are so plagued by bloated payrolls, antiquated equipment, and corrupt management that lower labor costs alone are unlikely to quickly restore their profitability. Finally, the devaluation probably will not promote much import-substitution: Gabon's small domestic market—the country's population is just over 1 million—restricts the development of efficient economies of scale. [REDACTED]

On the negative side, the CFA devaluation will add significantly to inflation and place significant new demands on government resources. The country imports over 90 percent of its consumer and capital goods—including food—which will all double in cost when the government lifts price controls. Price controls have already created shortages of pharmaceuticals and other goods. At least until salaries can catch up with

~~Secret~~

~~Secret~~

this inflationary shock, the real purchasing power of the average Gabonese will fall, as will the real value of government revenue, especially because Libreville has promised to hold down tariff rates to cushion the blow of devaluation. [REDACTED]

Heightened Prospects for Civil Unrest

In our view, the devaluation increases the risk that the current tensions over democratization could become violent, but such unrest is unlikely to threaten the regime. Gabonese took to the streets to protest economic downturns in the mid-1980s and in 1990 over reductions in health care subsidies. [REDACTED] believes prospects are good this time that civilians will violently protest their loss of purchasing power. Although Bongo historically has not violently suppressed popular protests, the military has assumed a much more visible security presence since the election. Bongo might see popular protests against devaluation as linked to his political opponents challenging the legality of his election and be more likely to crack down further. [REDACTED]

Implications for the United States

The devaluation is likely to increase tensions already present in Gabonese-US bilateral relations. The Bongo government has recently escalated its verbal attacks against the United States, claiming that Washington is meddling in Gabon's internal affairs by supporting Bongo's opponents and criticizing its restrictions on opposition travel. Washington's outspokenness on the need for devaluation and the lack of assistance from international financial institutions, which are viewed as heavily influenced by Washington, are likely to make the United States a scapegoat for the devaluation's negative effects. [REDACTED]

The US trade deficit with Gabon will probably grow moderately as a consequence of the devaluation. US imports of oil from Gabon—amounting to about \$1 billion in 1992—probably will continue at similar levels. But US exports to Gabon, which are concentrated in specialized oil and mining equipment, are likely to become prohibitively expensive. [REDACTED]

[REDACTED]

~~Secret~~

~~Secret~~

Mali: Sharing the Pie Among Noisy Economic Interests

The 18-month-old democratically elected government of President Konare is anticipating a potentially violent response to the devaluation of the CFA franc, but it will probably survive the crisis. Landlocked and arid, Mali is heavily dependent on imports, including staple foods, and volatile urban groups will be most vulnerable to higher import prices. Although the government hopes to continue reform measures that will foster diversification of the economy and attract foreign investment, widespread unrest could force Konare to backtrack on key austerity measures. Bamako is already under scrutiny by international financial institutions for failure last year to control government expenditures. It now will seek relief from pressures to reduce its deficit as it tries to satisfy the financial demands of labor, student, and military groups. The Konare government will expect donor help in maintaining the peace.

A Difficult Economic and Political Balancing Act

The lack of major economic resources complicates Bamako's efforts to satisfy competing political interests and to raise the country's low standard of living. The economy revolves around subsistence agriculture and animal husbandry, and earns revenues from only a few exports, mainly cotton, livestock, and gold. In 1993, Mali had to import some 45,000 metric tons of cereals, and remains totally dependent on imports for petroleum products.¹ The government had run up a massive deficit as of the middle of last year.

Bamako had dragged its feet on necessary cuts in wages and subsidies that affect key urban interest groups, such as labor and students, because of fears of public protests. Although the cost of stipends for some 8,000 students exceeds national expenditures for health care, students rioted last April, burning part of the capital, to protest government interference in student union politics and other grievances. Bamako's heavy dependence on external financing has compelled it to cooperate more closely

with the IMF and World Bank in recent years, and it has made a strong effort to privatize major state-owned industries, such as mining, tanning, and textiles. In late 1993, the IMF and World Bank suspended aid to Mali for failing to curb government expenditures, but subsequent budget reforms have partially satisfied the international lenders' recommendations.

Despite Konare's widely recognized legitimacy and relative popularity, he has had problems maintaining a governing consensus on key issues. In a nod to the contributions made by other players—students, for example—in the 1991 ouster of dictator Moussa Traore, Konare has chosen to govern with the cooperation of a coalition of six parties despite the majority his Association for Democracy in Mali has in the legislature. The President has changed prime ministers once—following criticism of the government's response to the student riots—shuffled the cabinet twice, and has come under fire from his own party for allowing the minority parties to influence his policies. Although the 1992 National Pact has largely stopped attacks in the north by organized ethnic Tuareg insurgents, some of whom have been integrated into the Malian armed forces, sporadic banditry by splinter groups—serious enough last year to temporarily drive relief organizations from the region—still occurs. Moreover, Tuareg leaders continue to believe that southern ethnic groups receive greater favor and fault Bamako for slow implementation of plans to improve the north's economy.

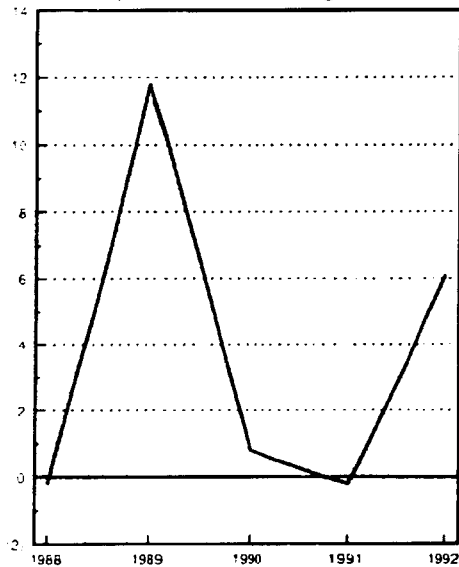
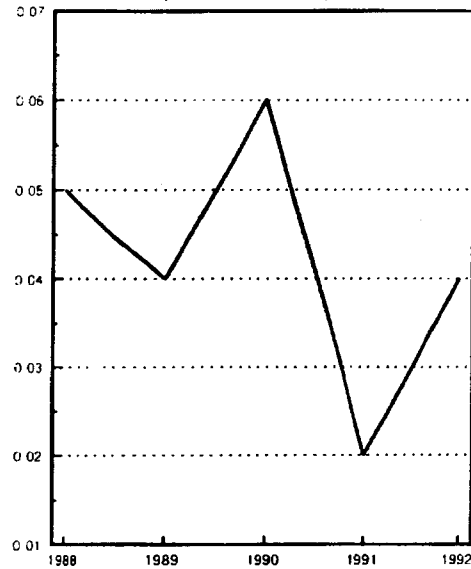
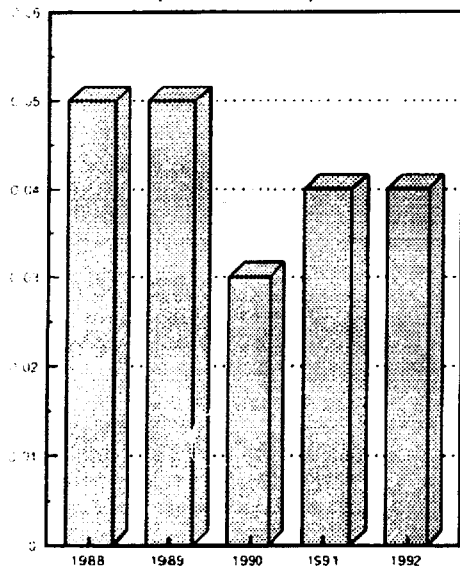
Initial Responses to the Devaluation

The government so far has failed to explain the potential benefits of devaluation to the public, but it moved rapidly when the announcement was made to try to dampen the business community's urge to raise prices and to deter hoarding. Malian officials reminded the public that all sectors would be sharing the burden of the devaluation, but that debt relief from France would ease the load. In agreement with the Chamber of

¹ Imports for 1991, the latest year for which figures are available, were \$600 million, with France the primary supplier. U.S. exports to Mali that year totalled \$26 million.

~~Secret~~

ALA AR 94-002
4 February 1994

~~Secret~~**Mali: Economic Indices****Real GDP**
(Annual Percent Change)**Current Account Balance**
(In Percent GDP)**Overall Deficit**
(In Percent GDP)~~Secret~~

~~Secret~~

Commerce, Bamako imposed a 15-day freeze on the prices of public utilities and local goods—flour, wheat, cooking oil, soap, milk, sugar, tea, and pharmaceuticals—and lifted tariffs on rice and sugar; the government promised to help companies settle increased debts owed to foreign suppliers. The Finance Minister informed foreign donors that the price freeze would not be vigorously enforced, that the market soon would be allowed to determine prices, and that businesses could not expect the government to bail them out. On 29 January the cabinet adopted a series of decrees that reduced import and income taxes, allowed limited price increases for certain commodities, slightly raised public sector salaries and student stipends, and increased farm prices. [REDACTED]

Initial public reactions have been largely negative, but relatively nonviolent. The Embassy says that many stores either doubled prices or closed in the first few days after the devaluation. Compliance on the initial price freeze was spotty; for example, the cost of sugar, cooking oil, tea, flour, and milk has risen between 15 and 50 percent at the retail level and prices for imported manufactured goods and luxury items have increased as much as 100 percent. A few shops were damaged by unorganized small groups of irate Malians and a merchant was rumored to have been killed. Despite the Prime Minister's attempt to placate students, they are demanding a 50-percent increase in their stipends and changes in the allocation of stipend money and on 2 February mounted a demonstration. The National Union of Malian Workers (UNTM) labor federation last week demanded that Mali leave the CFA and restore its own currency. It called for 50-percent salary increases, payment of salary arrears, a pension increase, and a higher minimum wage. Television and radio workers called a 48-hour strike. [REDACTED]

The impact of the devaluation may be somewhat alleviated by donor debt forgiveness and other concessions, since Mali is ranked by the World Bank as among the "poorest" countries. As part of the devaluation package, France has agreed to cancel all outstanding development assistance loans to poor countries in the region, but countries will then have to agree to a structural adjustment program supported by the IMF to obtain new financing. Paris also has promised to establish a special development fund for franc zone countries with an initial grant pool of

300 million French francs that will emphasize improving employment opportunities, education, and health. The Embassy said in late January that Bamako would soon sign a letter of intent with the IMF if differences over civil service salary increases are resolved as expected. The agreement would allow Mali to draw on the next \$28 million tranche of the enhanced structural adjustment facility that was suspended last year. [REDACTED]

Mali's Leaders and the Devaluation

Although President Konare—a former publishing magnate, archaeologist, and historian—apparently had qualms about devaluation, he will try to make the best of it and is committed to going through with needed economic reforms. [REDACTED]

Interviewed last December, Konare expressed impatience to see the devaluation question resolved one way or another as long as CFA countries remained united on the issue. [REDACTED] blamed the CFA members for [REDACTED]

Economic Benefits Too Far Down the Road?

Because Mali is dependent on imports for key staple commodities and exports only a few products, the impact of the devaluation in the short term is likely to be negative, and urban groups probably will step up pressure on the government to cancel or modify parts of its economic reform program. If the government follows through on promises to allow price controls to lapse quickly, resulting inflation will hit urban dwellers hard, particularly traders, salaried workers, civil servants, students, and military enlisted men. These groups will press for abrogation of donor-recommended caps on civil service salaries and fringe benefits and elimination of new strict requirements for student benefits. Initial attempts to aid importers by holding down tariffs or helping to alleviate private sector foreign debt will reduce Bamako's ability to increase

~~Secret~~

~~Secret~~

revenues; the large budget deficit already was projected to rise by 11 billion CFA in 1994 at the former exchange rate. In addition, [REDACTED] attempts to control fraud will be hindered as monitoring officials responsible for measures such as price controls are offered inducements to ignore violations. [REDACTED]

Although rural agricultural producers could benefit from improved prices for their products and the unemployed from new jobs created by foreign investors, most Malians will be unable to take advantage of positive aspects of the devaluation. Many Malians misunderstand devaluation and will be slow to seize business opportunities. A local tea producer, for example, lamented to Embassy officials about the devaluation, but failed to realize that his tea would be more competitive. Moreover, Mali's principal exports, especially cotton and gold, will continue to require foreign-supplied materials and machinery. An economist from the cotton company estimated that the increased cost of inputs would significantly reduce the benefits of increased exports. [REDACTED] In addition, Mali's relatively high long-term interest rates—15 percent or more—hinder business expansion and will come down only slowly, in our judgment, if, as expected, bank deposits are reduced in response to the uncertain exchange situation. [REDACTED]

Will Malians Take to the Streets?

Mali almost certainly will witness at least sporadic unrest in response to the new economic pressures, and any incident could escalate to the level of last year's student violence or worse.² Students remain particularly volatile even though Bamako has maintained stipends; scholarships have become more difficult to obtain and the availability of school places, teachers, and books has declined with government budget cuts. The UNTM, although currently reluctant to do so, may call a general strike that could become violent. Intermittent labor strikes are a certainty in any case and are already occurring. In addition, street crime is likely to increase—it has grown by 25 to 50 percent in the past year [REDACTED] and inadequate police staffing and training, worsened by budget cuts, will make it difficult to contain. Economic

problems also will make it harder to satisfy the demands of groups like the Tuareg, some of whom may return to the battlefield. [REDACTED]

There may be a greater threat from the military as rank-and-file troops calculate the effect of the devaluation on their already low living standards and on military readiness should the north revert to insurgency. Unfamiliar civilian Defense Ministry leadership, poor living conditions, and the integration program for Tuareg rebels have fueled growing dissatisfaction with the Konare government among the enlisted ranks over the past year. [REDACTED]

The "Coordination," a powerful unofficial union of noncommissioned officers (NCOs), has successfully used its considerable influence to try to wrest costly benefit concessions—most recently on retirements—from the government. In December, the government announced that it had foiled a plot—by NCOs and a jailed former chief aide to dictator Traore—to assassinate Konare and overthrow the government. [REDACTED]

Can the Konare Government Handle the Crisis?

We believe Konare probably can weather the immediate reaction to devaluation, but a long battle of attrition could undermine the fragile government coalition and national consensus for the democratic experiment. The government probably will adopt time-tested tactics of caucusing with and cajoling the various interest groups and giving in partially—but not fully—to some demands. After the 1993 student riots, the government was criticized by political opponents for not acting forcefully enough to stop the destruction, but its decision not to use lethal force almost certainly helped prevent escalation of the violence. The government also has held the line against replacing the civilian defense minister with a military officer. Konare's opponents—even in the military—undoubtedly realize they must continue with democracy to retain vital donor assistance, but his honeymoon is over, and he is likely at a minimum to hear calls for his resignation from the public and government ranks, and perhaps face more coup plotting if the economic crisis sparks civil unrest. [REDACTED]

²Antigovernment violence in 1991 preceding Traore's downfall cost 200 lives and \$145 million in property damage. [REDACTED]

~~Secret~~

~~Secret~~**Implications for Washington**

Bamako will be casting the net widely for foreign aid and investment, with an emphasis on support for job creation and the expansion of inadequate educational facilities, that may help defuse urban tensions without abandoning plans to help improve the lot of the northern Tuareg. It will expect donors to maintain grant aid on a permanent basis. Konare is committed to maintaining good relations with international and bilateral lenders by carrying out economic reforms, but his efforts to rule by consensus demand that he not take an inflexible position against key interest groups. He probably will expect donors to lessen their pressure for budget cuts as a reward for Mali's cooperation on devaluation and continued commitment to democratic rule. Reforms like privatization of state corporations will continue, however, providing opportunities for US and Western investors to buy in or set up shop at a more favorable exchange rate. Foreign investors, including some US interests, already have a stake in several gold-mining operations. US exports to Mali, in contrast, probably will suffer; the US market share in Mali increased 400 percent in the last decade, but devaluation will make buyers less receptive unless Malian importers receive exceptionally favorable credit terms from US suppliers.

[REDACTED]

~~Secret~~ALA AR 94-002
4 February 1994